Supreme Court, U.S.
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No. _____

In the
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 2006

BRUCE COMLY FRENCH, Trustee for the Debtor Estate of Ernest Bergman and Shirley E. Bergman, Petitioner,

v.

STEVE FREY: ANTHEM BLUE CROSS AND BLUE SHIELD; AND GERMAN MUTUAL INSURANCE COMPANY, Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

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PETITION FOR A WRIT OF CERTIORARI

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January 23, 2007

QUESTIONS PRESENTED

Whether the Court of Appeals relegated a significant federal interest when it interpreted Section 541 of the Bankruptcy Code to exclude from the definition of property of the Estate all funds recovered by the Trustee for the benefit of the Estate which might be due to third parties under non-bankruptcy law.

LIST OF PARTIES

The debtors Ernest R. and Shirley E. Bergman, through the Trustee in Bankruptcy, Bruce Comly French, constitute the plaintiffs below. Defendants include the alleged tortfeasor, Steve Frey, and two insurance companies who have made payments on behalf of Frey to the Bergmans, Anthem Blue Cross and Blue Shield and German Mutual Insurance Company.

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IN THE SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 2006

PETITION FOR A WRIT OF CERTIORARI

Petitioner, Bruce Comly French, Trustee for the Debtor Estate of Ernest R. and Shirley E. Bergman, respectfully requests that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Sixth Circuit, entered on October 27, 2006 in Bruce Comly French, Trustee, etc. v. Steve Frey, *et al.*

OPINIONS BELOW

The opinion and judgment of the United States Court of Appeals for the Sixth Circuit is published at 467 F.3d 536 (6th Cir. 2006). It is reprinted in the appendices herein, p. 1a, *infra*.

The order of the United States District Court for the Northern District of Ohio is published at 337 B.R. 616 (N.D. Ohio 2005). It is reprinted in the appendices herein, p. 11a, *infra*.

JURISDICTION

On March 14, 2005, the Trustee for the Debtor Estate of Ernest R. and Shirley E. Bergman [hereafter, "Trustee"] filed his Adversary Proceeding in the United States Bankruptcy Court for the Northern District of Ohio against Anthem Blue Cross and Blue Shield and German Mutual Insurance Company [hereafter, "insurance companies"], pursuant to 28 U.S.C. Sections 157, 1334, 2201, and 2002, to have that court treat any subrogation claim of the insurance companies as that of a general unsecured creditor under

Section 726(a)(2) of the Bankruptcy Code.

On March 17, 2005, the Trustee filed against the alleged tortfeasor Steve Frey who caused personal injuries against the debtors a complaint for the debtors' personal injuries, seeking $100,000.00, plus costs, pursuant to 28 U.S.C. Sections 157 and 1334.

At the initial hearing involving both of these cases, the Bankruptcy Court entered on April 19, 2005, its Order of Consolidation. On July 26, 2005, the District Court withdrew the order of reference of these, now consolidated, cases, given Frey's demand for a jury trial.

The District Court thereafter entertained the Trustee's Motion for Judgment on the Pleadings with regard to the subrogation issue and the cross-motion for summary judgment by the insurance companies.[1] The District Court granted on September 22, 2005, the motion for summary judgment.

An appeal to the United States Court of Appeals for the Sixth Circuit, pursuant to 28 U.S.C. Section 1291, was perfected on or about October 3, 2005.

The United States Court off Appeals on October 27, 2006, entered its judgment affirming the grant of summary judgment in favor of the insurance companies.

This petition for certiorari is timely filed pursuant to 28 U.S.C. Section 1254(1) to review the judgment of the

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[1] Although only Anthem Blue Cross and Blue Shield briefed this issue, all parties below understood that a judgment in favor of the Trustee or Anthem Blue Cross and Blue Shield bound all other parties.

Court of Appeals.

STATUTORY PROVISIONS INVOLVED;

11 U.S. Code Section 541 provides, *inter alia*:

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is—

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date—

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

(b) Property of the estate does not include—

(1) any power that the debtor may exercise solely for the benefit of an entity other than the debtor;

(2) any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease before the commencement of the case under this title, and ceases to include any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease during the case;

(3) any eligibility of the debtor to participate in programs authorized under the Higher Education Act of 1965 (20 U.S.C. 1001 *et seq.*; 42 U.S.C. 2751 *et seq.*), or any accreditation status or State licensure of the debtor as an educational institution;

(4) any interest of the debtor in liquid or gaseous hydrocarbons to the extent that—

(A)(i) the debtor has transferred or has agreed to transfer such interest pursuant to a farmout agreement or any written agreement directly related to a farmout agreement; and

(ii) but for the operation of this paragraph, the estate could include the interest referred

to in clause (i) only by virtue of section 365 or 544(a)(3) of this title; or

(B)(i) the debtor has transferred such interest pursuant to a written conveyance of a production payment to an entity that does not participate in the operation of the property from which such production payment is transferred; and

(ii) but for the operation of this paragraph, the estate could include the interest referred to in clause (i) only by virtue of section 365 or 542 of this title; or

(5) funds placed in an education individual retirement account (as defined in section 530(b)(1) of the Internal Revenue Code of 1986) not later than 365 days before the date of the filing of the petition in a case under this title, but—

(A) only if the designated beneficiary of such account was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were placed in such account;

(B) only to the extent that such funds—

(i) are not pledged or promised to any entity in connection with any extension of credit; and

(ii) are not excess contributions (as described in section 4973(e) of the Internal Revenue Code of 1986); and

(C) in the case of funds placed in all such accounts having the same designated beneficiary not earlier than 720 days nor later then 365 days before such date, only so much of such of such funds as does not exceed $5,000;

(6) funds used to purchase a tuition credit or certificate or contributed to an account in accordance with section 529(b)(1)(A) of the Internal Revenue

Code of 1986 under a qualified State tuition program (as defined in section 529(b)(1) of such Code) not later than 365 days before the date of filing of the petition in a case under this title, but—

(A) only if the designated beneficiary of the amounts paid or contributed to such tuition program was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were paid or contributed;

(B) with respect to the aggregate amount paid or contributed to such program having the same designated beneficiary, only so much of such amount as does not exceed the total contributions permitted under section 529(b)(7) of such Code with respect to such beneficiary, as adjusted beginning on the date of the filing of the petition in a case under this title by the annual increase or decrease (rounded to the nearest tenth of 1 percent) in the education expenditure category of the Consumer Price Index prepared by the Department of Labor; and

(C) in the case of funds paid or contributed to such program having same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $5,000;

(7) any amount—

(A) withheld by an employer from the wages of employees for payment as contributions—

(i) to—

(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section

414(d) of the Internal Revenue Code of 1986;

(II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or

(III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986; except that such amount under this subparagraph shall not constitute disposable income as defined in section 1325(b)(2); or

(ii) to a health insurance plan regulated by State law whether or not subject to such title; or

(B) received by an employer from employees for payment as contributions—

(i) to—

(I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;

(II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or

(III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986; except that such amount under this subparagraph shall not constitute disposable income as defined in section 1325(b)(2); or

(ii) to a health insurance plan regulated by State law whether or not subject to such

title;

(8) subject to subchapter III of chapter 5, any interest of the debtor in property where the debtor pledged or sold tangible personal property(other than securities or written or printed evidences of indebtedness or title) as collateral for a loan or advance of money given by a person licensed under law to make such loans or advances, where—

(A) the tangible personal property is in the possession of the pledgee or transferee;

(B) the debtor has no obligation to repay the money, redeem the collateral, or buy back the property at a stipulated price; and

(C) neither the debtor nor the trustee have exercised any right to redeem provided under the contract or State law, in a timely manner as provided under State law and section 108(b); or

(9) any interest in cash or cash equivalents that constitute proceeds of a sale by the debtor of a money order that is made—

(A) on or after the date that is 14 days prior to the date on which the petition is filed; and

(B) under an agreement with a money order issuer that prohibits the commingling of such proceeds with property of the debtor (notwithstanding that, contrary to the agreement, the proceeds may have been commingled with property of the debtor),

unless the money order issuer had not taken action, prior to the filing of the petition, to require compliance with the prohibition.

Paragraph (4) shall not be construed to exclude from the estate any consideration the debtor retains, receives, or is entitled to receive for transferring an interest in liquid or gaseous hydrocarbons pursuant to a farmout agreement.

(c)(1) Except as provided in paragraph (2) of this subsection, an interest of the debtor in property becomes property of the estate under subsection (a)(1), (a)(2), or (a)(5) of this section notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law—

(A) that restricts or conditions transfer of such interest by the debtor; or

(B) that is conditioned on the insolvency or financial condition of the debtor, on the commencement of a case under this title, or on the appointment of or taking possession by a trustee in a case under this title or custodian before such commencement, and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property.

(2) A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.

(d) Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such a mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

(e) In determining whether any of the relationships specified in paragraph (5)(A) or (6)(A) of subsection (b) exists, a legally adopted child of an individual (and a child who is a member of an individual's household, if placed with such individual by an authorized placement agency for legal

adoption by such individual), or a foster child of an individual (if such child has as the child's principal place of abode the home of the debtor and is a member of the debtor's household) shall be treated as a child of such individual by blood.

(f) Notwithstanding any other provision of this title, property that is held by a debtor that is a corporation described in section 501(c)(3) of the Internal Revenue Code of 1986 and exempt from tax under section 501(a) of such Code may be transferred to an entity that is not such a corporation, but only under the same conditions as would apply if the debtor had not filed a case under this title.

STATEMENT OF THE CASE

On or about March 22, 2003, Ernest R. and Shirley E. Bergman were involved in Franklin County, Ohio, in an automobile wreck with Steve Frey. Medical bills were paid on behalf of Frey to the Bergmans by the insurance carriers in an approximate sum slightly exceeding $10,000.00.

On August 8, 2003, the Bergmans filed a petition for voluntary bankruptcy under chapter 7 of the Bankruptcy Code in the United States Bankruptcy Court for the Northern District of Ohio, Western Division at Toledo. Bruce Comly French was appointed by the Office of the United States Trustee Region IX, U. S. Department of Justice, as the interim Trustee for the Bergman's bankruptcy.

On March 17, 2005, the Trustee timely filed in the Bankruptcy Court his personal injury suit against Frey. Days before, he had filed his suit (essentially a declaratory judgment action) against the insurance companies to have any claim for recovery they might have from the Trustee's successful suit against the third party tortfeasor Frey limited

to their standing in the shoes of a general unsecured creditor—rather than allowing them to take directly from any proceeds realized from the suit against Frey. Whether the insurance companies took off the top (from the personal injury settlement) or off the bottom (as a general unsecured creditor in the claims' distribution process of the Bankruptcy Court) was a significant factor in the Trustee's statutory obligation to ensure the fair treatment of all creditors under the priority payment scheme Congress adopted as Section 507 of the Bankruptcy Code.

The Trustee seeks a reversal of the order of the Court of Appeals, the subsequent vacation of the District Court's granting of the insurance companies' motion for summary judgment, and further consideration, thereafter in the District Court, of the Trustee's Motion for Judgment on the Pleadings.

THE WRIT OF CERTIORARI SHOULD ISSUE TO PROPERLY INTERPRET THE PROVISIONS OF SECTION 541 OF THE BANKRUPTCY CODE

A. Overview of Argument.

The courts below have improperly and narrowly interpreted the federal interest in a broad definition of property of the Estate set forth in Section 541 of the Bankruptcy Code. This case provides the opportunity to define broadly the term "property" in accordance with the intentions of the Congress in its enactments so as to maximize the funds available for the just and equitable payment of monies to all creditors in accordance with the Congressional scheme for the payment of Estate obligations.

B. Property of the Bankruptcy Estate is Expansively Defined by the Congress.

Section 541 of the Bankruptcy Code, set forth above, is a wide, expansive definition. Section 541(a) defines property in as many ways as is possible to be all inclusive. No doubt exists as to the inclusion of personal injury claims within the ambit of subsection (a). *Wischan v. Adler* (*In re Wischan*), 77 F.3d 875 (5th Cir. 1996). *See, also*, COLLIER ON BANKRUPTCY Section 541.08[2] (15th. ed.)

C. Congress Is Able to Limit the Reach as to What Constitutes "Property" When It Chooses to Do So.

Section 541(b), set forth above, provides a limited number of exemptions from the broad definition of property in subsection (a). None of the exemptions enacted by the Congress has the slightest relevance to the monies at issue in the instant litigation.

The Court has determined that property under certain non-bankruptcy acts adopted by the Congress, such as the Employee Retirement Income Security Act of 1974, (Pub. L. 93-406), as amended, are not property of the Estate. *Patterson v. Shumate*, 504 U.S. 753 (1992).

This Court should be wary of adding to the list of property deemed not to be Estate property when the Congress has shown its ability to create the list it desired.

D. This Court's Recent Pronouncements of the Significance of the Bankruptcy Clause in Article I of the Constitution Compel a Reexamination of Decisions Which Limit the Reach of Congress's Intentions in the Bankruptcy Context.

This Court's recent decision in *Katz v. Central Virginia Community College* (*In re Wallace Bookstores*), 126 S. Ct. 990 (U.S. Jan. 23, 2006) emphasized the centrality of the several States' surrender of state authority in the

bankruptcy context. Even when faced with strong precedent under the Eleventh Amendment in the context of state immunity from many suits, the Court reasoned that the Bankruptcy Clause warranted solicitous treatment and that provisions purporting to waive state immunity in Section 106 of the Bankruptcy Code were, in fact, constitutional.

E. Statutory Amendments Affecting the Bankruptcy Code Which Follow Narrower Interpretations of the Definition of Property under Earlier Code Provisions Require that the Federal Interest in a Broad Definition of Property Be Revisited.

Significant amendments to the Bankruptcy Code in the Bankruptcy Reform Act of 1978, (Pub. L. 95-598), as amended, (2005) and the more recent, Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. 109-8, as amended, (2005), maintaining a broad, expansive definition of Estate property require that the Court be vigilant in reining in lower court decisions that limit Congress's definition.

F. *Pearlman v. Reliance Insurance Company*, Cited as Controlling Authority to the Contrary Below, Has No Relevance to the Definition of Property at Issue in this Case.

Both lower courts relied upon *Pearlman v. Reliance Insurance Co.*, 371 U.S. 132 (1962) as controlling the outcome of this litigation. *Pearlman* is a venerable case; it just is not involved with the subrogation issue presented in this case. In *Pearlman*, the referee (now, trustee) in bankruptcy, sought to receive monies from a surety bonding company alleged to be Estate property. The surety bond, required by the federal Miller Act under the facts set forth in Mr. Justice Black's opinion for the Court in *Pearlman*, became the basis for the completion of the public works project undertaken by the referee's predecessor-in-interest.

Simply, then, the job would not have occurred in *Pearlman*, had not the surety bond been available to get the job done.

Under the facts presented in *Pearlman*, the result seems unassailable, although one member of the Court dissented (371 U.S. at 142) and three Justices concurred in the result, reading more narrowly the several precedential cases (371 U.S. at 142-144).

G. Claims of Subrogated Parties Are Not like the Special Suretyship Cases, but Rather General Unsecured Claims.

The factual matters in issue here bear no resemblance to the *Pearlman* facts. Rather, the facts here look more like a credit card transaction—a transaction, contractual in nature, which all would agree results in providing for a general, unsecured debt under the bankruptcy claims' payment scheme enacted by the Congress. The credit issuer agrees to pay the retailer, for example, when the customer decides to buy on his or her credit card an item offered for sale by the retailer. The customer gets the item; the credit card issuer is to pay the retailer (less some small transactional costs); and the credit card issuer subsequently bills the customer for payment. Should the customer become a debtor under the Bankruptcy Code, then the credit card issuer will only receive funds obtained by the Trustee and made available for distribution to it as a general unsecured creditor in accordance with Congress's payment scheme. If no monies, or insufficient monies, are obtained by the Trustee, the credit card issuer will receive a *pro rata* distribution, or, more likely, nothing with the usual no-asset case. So much for the credit card issuer's contractual right to be made whole.

Here, the trustee's predecessors-in-interest, the debtors Bergmans, were involved in a traffic wreck with Mr. Frey. Medical care resultant from the wreck was provided by sundry health care providers. In this example, the health care

providers are like the retailer in the prior paragraph's example. The two defendants below (respondents here) paid the health care provider "retailer" like the credit card issuer in the prior paragraph's example. Should no suit be filed against the third party tortfeasor who caused the wreck, the insurance companies interest is inchoate and they get nothing —other than, perhaps, the satisfaction of helping their injured victim toward full recovery.

When the trustee files suit, should he or she determine it is in the interests of all of the Estate's creditors to do so, then the insurance carriers have a choate claim which might ripen into something of value. What the insurance carrier should get is that what Congress promised to general unsecured creditors—that they would be paid at the second level of preference under Section 726 of the Bankruptcy Code. And that is what these respondents should get as well —and nothing more.

H. Interpretations of Ohio Law by Its Supreme Court and Comments about Its Pronouncements by the Bankruptcy Courts Are *Obiter Dicta* When Viewed in the Context of Federal Bankruptcy Law.

The Court of Appeals for the Sixth Circuit noted that the subrogation clause at issue in this litigation had been interpreted in substantial part by the Supreme Court of Ohio in *Blue Cross and Blue Shield Mutual Ohio v. Hrenico*, 72 Ohio St.3d 120, 647 N.E.2d 1358 (1995). While subsequent decisions of the Supreme Court of Ohio had explained and distinguished the *Hrenico* decision, *see Northern Buckeye Education Council Group Health Benefits Plan v. Lawson*, 103 Ohio St.3d 188, 814 N.E.2d 1210, 1215-1216 (2004), the state supreme court's views of Ohio state contract and insurance law is entitled to deference. However, it is not at all binding in the context of litigation which involves the federal definition of property, *not* the state definition of

property. Similarly, the Bankruptcy Court decision in *Ginley v. Blue Cross and Blue Shield of Ohio* (*In re DuBose)*, 174 B.R. 260 (Bankr. N. D. Ohio 1994), likely represents a correct understanding of Ohio law, but it is not controlling and must be viewed as *obiter dicta* in the context of federal bankruptcy law.

I. Conclusion.

The issues fairly presented by this case call out for this Court's consideration so that the preemptive federal bankruptcy policy of a broad, expansive definition of Estate property may be vindicated. Any limitations to that broad definition must be those chosen by the Congress, and by it alone.

CONCLUSION

For the foregoing reasons, the petitioner requests that a writ of certiorari issue to the United States Court of Appeals for the Sixth Circuit to provide the relief sought by the petitioner.

Respectfully submitted,

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UNITED STATES COURT OF APPEALS

FOR THE SIXTH CIRCUIT

In re: ERNEST R. BERGMAN; SHIRLEY E. BERGMAN,

Debtors.

No. 05-4312

BRUCE COMLY FRENCH, Trustee for the Debtor Estate of Ernest Bergman and Shirley E. Bergman,

Plaintiff-Appellant,

v.

STEVE FREY; ANTHEM BLUE CROSS AND BLUE SHIELD; GERMAN MUTUAL INSURANCE COMPANY,

Defendants-Appellees.

Appeal from the United States District Court
for the Northern District of Ohio.
Nos. 05-07311; 05-07310—
James G. Carr, Chief District Judge.

Submitted: September 12, 2006

Decided and Filed: October 27, 2006

Before MERRITT and MOORE, Circuit Judges; COLLIER, Chief District Judge.*

COUNSEL

ON BRIEF: Bruce Comly French, Lima, Ohio, Ryan Q. Ashworth, Ada, Ohio, for Applellant. Louis F. Solimine, THOMPSON HINE, Cincinnati, Ohio, Curtis L. Tuggle, THOMPSON HINE, Cincinnati, Ohio, for Appellees.

OPINION

MERRITT, Circuit Judge. On March 23, 2003, prior to filing bankruptcy, Ernest and Shirley Bergman were involved in an automobile accident. The Bergmans' medical insurer, Anthem Blue Cross and Blue Shield provided coverage for approximately $3,000 in medical expenses incurred by the couple arising from the accident. After the Bergmans filed a Chapter 7 bankruptcy petition, the trustee initiated a personal injury lawsuit on behalf of the debtor estate against Steve Frey, the other party to the automobile accident, seeking in excess of $100,000 in damages. The issue in the present action is whether Anthem, via a subrogation clause in the Bermans' insurance policy, acquired a pre-petition interest in the first $3,000 the Bergmans my obtain from Frey. The District Court held that it did. The Trustee argues that Anthem did not acquire a pre-petition interest and that the insurer should properly be

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* The Honorable Curtis Lynn Collier, Chief United States District Judge for the Eastern District of Tennessee, sitting by designation.

classified as a general unsecured creditor. For the reasons explained below, the decision of the District Court is affirmed.

The Bergmans' insurance policy includes a subrogation clause, which provides:

> We [Anthem] have the right to recover payments we make on your behalf from any party responsible for compensating you for your injuries. The following apply: We have first priority for the full amount of benefits we have paid from any recovery regardless of whether you are fully compensated, and regardless of whether the payments you receive make you whole for your losses and injuries.

After the bankruptcy commenced, the Trustee filed a personal injury suit on behalf of the debtor estate against Frey, seeking more than $100,000 in damages. The Trustee also initiated an adversary complaint against Anthem, asking the bankruptcy court to declare the Bergmans' insurer a general unsecured creditor. The Bankruptcy Court consolidated both actions into a single proceeding and the District Court withdrew the case from the Bankruptcy when Frey demanded a jury trial. In the District Court, the Trustee moved for a judgment on the pleadings and Anthem cross-moved for summary judgment. The District Court granted Anthem's motion, holding that under Ohio law the insurer had a pre-petition property interest in any recovery that the Bergmans may receive arising out of their accident with Frey.

We review the District Court's grant of summary judgment de novo. The issue presented is whether an insurer's contractual subrogation rights create a property right in the insurer, so that this contractual right is not properly included in the bankruptcy estate. The Bankruptcy Code defines the property of the debtor's estate as "all legal or equitable interests of the debtor in property at the outset of the case." 11 U.S. C. § 541 (a)(1). Unless a federal interest is at issue, property rights are defined by state law. *Butner v. United States*, 440 U.S. 48, 55 (1970). Here, the court must look to state law to determine whether, at the outset of the Bergmans' bankruptcy case, the debtors possessed a legal or equitable interest in any potential recovery from Steve Frey.

The Ohio Supreme Court confronted this issue outside the bankruptcy context in a dispute between a medical insurer and its insured in Blue Cross and Blue Shield v. Hrenko, 647 N.E.2d 1358 (1955). In Hrenko, the insurer paid for medical expenses incurred by its insured as a result of an automobile accident. The other party to the accident was not insured, so Hrenko pursued a claim under the uninsured motorist provision in his automotive insurance policy. The medical insurance company sued, arguing that the policy's subrogation clause entitled it to reimbursement for the money it had expended on behalf of its insured.[1] The Supreme Court agreed, rejecting Hrenko's arguments that his medical insurer's subrogation rights existed

1 The subrogation clause in Hrenko's policy stated, "To the extent we provide or pay for Covered Services, we assume your legal rights to any recovery of expenses incurred. To the extent we provide or pay benefits for Covered Services, you must repay us amounts recovered by suit, settlement or otherwise from any third party or his insurer." 649 N.E.2d at 1359.

exclusively against the tortfeasor or tortfeasor's insurer and that the insurer's subrogation rights were contrary to public policy. *Id.* at 1360. The Court held that the plain meaning of the contract language allowed the insurer to recover directly from compensation the insured received from any third party. *Id.* at 1359.

The subrogation rights conferred by contract are not affected by the Bankruptcy Code or the bankruptcy proceedings of the insured. In *Perlman* [sic] *v. Reliance Insurance Co.*, 371 U.S. 132 (1962), an insurance company provided surety bonds for a construction company that undertook a government project. *Id.* at 133. The bonds were to be used to compensate laborers and material suppliers at the project's conclusion if the company failed to meet its obligations. *Id.* As the project progressed, the government also retained a portion of the payments due to the constructions company under the contract. *Id.* at 134. Before the project was completed, the construction company terminated the contract and filed bankruptcy, leaving a second company to finish the work. *Id.* At the project's conclusion, the insurance company fulfilled its obligations by paying the full value of the surety bonds to creditors of the first construction company. *Id.* At this point the government turned over the money it had withheld under the contract to the Trustee for the bankrupt construction firm. *Id.*

The insurance company intervened in the bankruptcy claiming that the money belonged to it and not the bankruptcy estate under the subrogation clause in the surety bonds. *Id.* at 136. The Supreme Court enforced this subrogation clause, holding that "Property interests in a fund not owned by a bankrupt at the time of adjudication, whether complete or partial, legal or equitable, mortgages,

liens, or simple priority rights, are of course not part of the bankrupt's property and do not vest in the trustee." *Id.* at 135-36. Since the insurance company had a contractual right to subrogation before its insured filed bankruptcy, the Trustee could not properly acquire it for the benefit of the general creditors.

A more recent case, adjudicated under the Bankruptcy Code and Ohio law, reached the same result. In re DuBose, 174 B.R. 260 (Bankr. N.D. Ohio 1994). In Dubose, the husband debtor was involved in an automobile accident prior to the couple's bankruptcy filing. Like Anthem in the present case, Mr. Dubose's medical insurer covered medical expenses he incurred as a result of the accident. While their bankruptcy was pending, the debtors received a personal injury settlement from the other party to the accident and reimbursed their medical insurer pursuant to the subrogation clause in their policy. When the Trustee learned of the payment to the medical insurer, he moved to set aside the post-petition transfer for the benefit of the couple's unsecured creditors.

The Bankruptcy Court denied the Trustee's motion, finding that the monies owed to the insurance company under a subrogation clause were never part of the bankruptcy estate. The court reasoned that the subrogation clause rendered the payment to the medical insurer compensation for a "separate and independent cause of action between [the debtor's insurer] and the tortfeasor." *Id.* at 262 The court bluntly observed that "the Debtors did not have an interest in the transaction" between the tortfeasor and their insurer. *Id.*

Under Ohio law, Anthem acquired a pre-petition property right in any future recovery by the Bergmans

arising from the March 2003 accident as soon as it expended money for their medical care. *Hrenko* makes it clear that the property rights of an insurer are governed by the policy language. The subrogation clause in the Bergman's policy stated, ("We [Anthem] have the right to recover payments we make on your behalf from any party responsible for compensating you for your injuries." This language is the functional equivalent of the clause the Ohio Supreme Court found to create an enforceable property right in the Hrenko's medical insurer. Since the property right immediately vested in Anthem, it was not included in the Bergmans' bankruptcy estate under § 541 of the Bankruptcy Code.

This result comports with the Supreme Court's reasoning and result in *Perlman* [sic] where the language of the surety bond vested a property right in the bond's issuer outside of bankruptcy that put the money facially owed to the debtor beyond the reach of the Trustee. *DeBose* likewise supports the finding that the insurer owns an interest in the money recovered by the insured up to the amount of the insurer's expenses. Since this interest accrues to the insurer alone, it can never become part of the bankruptcy estate.

The Trustee argues that the policy language gives Anthem a right of reimbursement but not subrogation. This interpretation is not compatible with the plain meaning of the clause. The statement that Anthem "may recover payments," clearly indicates that it has the contractual right to seek payments directly. There is nothing in the clause that suggests that Anthem must wait until the Bergmans are compensated in order to enforce its rights under the policy. The Trustee is correct that the presence of a reimbursement clause, instead of the subrogation language, may alter this analysis. Such a reading of this clause, however, is not plausible.

For the foregoing reasons, we affirm the judgment of the district court.

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 05-4312

In re: ERNEST R. BERGMAN; SHIRLEY E. BERGMAN,
Debtors.

BRUCE COMLY FRENCH, Trustee for the Debtor Estate of Ernest Bergman and Shirley E. Bergman,
Plaintiff-Appellant,

v.

STEVE FREY; ANTHEM BLUE CROSS AND BLUE SHIELD; GERMAN MUTUAL INSURANCE COMPANY,
Defendants-Appellees.

Before: MERRITT and MOORE, Circuit Judges; COLLIER, Chief District Judge.

JUDGMENT

On Appeal from the United States District Court
for the Northern District of Ohio

THIS CAUSE was heard on the record from the district court and was submitted on briefs without oral argument.

IN CONSIDERATION WHEREOF, it is ORDERED that the judgment of the district court is AFFIRMED.

ENTERED BY ORDER OF THE COURT

/s/Leonard Green
Leonard Green, Clerk

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF OHIO
WESTERN DIVISION

Bruce Comly French, Trustee
for the Debtor Estates of
Ernest Bergman and
Shirley E. Bergman,

Plaintiff

v.

Steve Frey, et al.,

Defendant

Case No. 3:05CV7311
Con.sol case 3:5CV7310

ORDER

This case comes before me from the Bankruptcy Court, in which debtors, Ernest and Shirley Bergman, filed a Chapter 7 petition. Consolidated with this proceeding are the Bergmans' civil suit against defendant Steve Frey and a complaint seeking a declaration that the defendant insurance companies are general unsecured creditors.

Anthem Blue Cross and Blue Shield (Anthem) contends that the subrogation clause in the Bergmans' insurance policy entitles it to the amount of the expenditures it made on behalf of the Bergmans, who were injured in an accident with defendant Frey.[1] The Trustee on behalf of the

[1] The subrogation clause provides:

> We have the right to recover payments we make on your behalf from any party responsible for compensating you for your injuries. The following apply: We have first

Bergmans asserts that Anthem is simply a general unsecured creditor and is not entitled to full recovery.

This Court has jurisdiction pursuant to 28 U.S.C. §§ 157 and 1334.

Pending is plaintiff Trustee's motion for judgment on the pleadings to establish defendant Anthem as a general unsecured creditor and Anthem's cross-motion for summary judgment. For the following reasons, defendant's motion shall be granted and the plaintiff's motion shall be denied.

Background

After the Bergmans' March 22, 2003 accident with Frey, Anthem paid approximately $3,000 of their medical expenses. On August 8, 2003, the Bergmans filed a Chapter 7 bankruptcy petition. The Bankruptcy Court entered an order appointing Bruce Comly French as Trustee on March 8, 2005.

On March 14, 2005, the Trustee filed an adversary complaint seeking to have Anthem declared a general unsecured creditor. Three days later, the Trustee filed a personal injury complaint against Frey, seeking damages in excess of $100,000 relating to the automobile accident.

> priority for the full amount of benefits we have paid from any recovery regardless of whether you are fully compensated, and regardless of whether the payments you receive make you whole for your losses and injuries.

Def.'s Resp. Ex. A at 2.

The Bankruptcy Court entered an order on April 19, 2005 consolidating both suits into a single adversary proceeding. I then withdrew this case from the Bankruptcy Court in light of Frey's jury demand. Thereafter, the Trustee filed a motion seeking judgment on the pleadings to establish Anthem and German Mutual Insurance Company as general unsecured creditors under Fed. R. Civ. P. 12(c). Anthem responded and filed a cross-motion for summary judgment under Fed. R. Civ. P. 56.

Standard of Review

Summary judgment must be granted only if "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). The moving party always bears the initial responsibility of informing the district court of the basis for its motion. *Celotex Corp. v. Catrett*, 477 U.S. 317, 323 (1986). The burden then shifts to the nonmoving party who "must set forth specific facts showing that there is a genuine issue for trial." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 250 (1986) (quoting Fed. R. Civ. P. 5(e)). Once the burden shifts, the party opposing summary judgment cannot rest on its pleadings or merely reassert its previous allegations. It is insufficient "simply [to] show that there is some metaphysical doubt as to the material facts." *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 586 (1986). Rather, Rule 56(e) "requires the nonmoving party to go beyond the [unverified] pleadings" and present some type of evidentiary material in support of its position. *Celotex*, 477 U.S. at 324.

In deciding the motion for summary judgment, the evidence of the non-moving party will be accepted as true, all doubts will be resolved against the moving party, all evidence will be construed in the light most favorable to the non-moving party, and all reasonable inferences will be drawn in the non-moving party's favor. *Eastman Kodak Co. v. Technical Servs., Inc.*, 504 U.S. 451, 456 (1992).

Discussion

Plaintiff Trustee states that the issue here is whether defendant is entitled to creditor priory status as defined in § 507. The Trustee contends that Anthem is a general unsecured creditor because insurers are not identified in the Code as entities with priority status.

The issue here is not, however, whether Anthem has priority status. Rather, the issue is whether a subrogation clause in an insurance policy creates a pre-existing property right in an insurer, with the result that the subrogation claim is not deemed to belong to the bankrupt's estate. The Trustee fails to address this issue directly. Instead, the Trustee relies solely on the language of the Bankruptcy Code and the argument that it should be read, as Congress intends, narrowly. This argument cannot prevail.

The Bankruptcy Code defines property of a bankruptcy estate as "all legal or equitable interests of the debtor in property at the outset of the case." 11 U.S.C. § 541(a)(1). The question in this case is whether, at the commencement of the bankruptcy case, the debtors had a legal or equitable interest in potential recoveries from defendant Steve Frey. Although federal law governs bankruptcy proceedings, state law creates and defines the

property interests, absent any supervening federal interest. *Butner v. U.S.*, 440 U.S. 48, 55 (1979).

The Ohio Supreme Court addressed this issue in a similar situation between an injured party and the health insurance provider. In *Blue Cross and Blue Shield Mutual of Ohio v. Hrenko*, 72 Ohio St. 3d 120 (1995), the insurer paid for medical expenses on behalf of its insured for injuries resulting from an automobile accident. The insured collected $42,000 in a settlement with the tortfeasor. The insurance company demanded reimbursement and sued under the policy's subrogation and reimbursement.

Ruling for the insurer, the court relied on both contract principles and public policy to identify the rights involved. *Id.* at 122. The court held that allowing the injured to receive medical expenses from both his insurer and the tortfeasor would circumvent the subrogation clause and place him in a better position than he was in before the accident. *Id.* Ordering reimbursement, the court held that the insurer had an enforceable property right under the subrogation clause. *Id.* at 120.

Applying these principles to the insurance contract in this case leads to the same result. Under *Hrenko* Anthem's subrogation rights vested as soon as it paid the Bergmans' medical expenses. Thus, under state law, Anthem has a property interest in its contractually-established right to recover those expenses from a suit filed against the tortfeasor, Frey.

These rights are unaffected by the Bankruptcy Code or bankruptcy proceedings involving the insured. In *Pearlman v. Reliance Insurance Co.*, 371 U.S. 132 (1962), an insurance company wrote surety bonds for a construction

company working under a government contract. Pending completion of the project, the government retained a percentage of its payments to the construction company. *Id.* at 134.

The company failed to complete the project, and filed bankruptcy. The insurer paid over $350,000 on the bonds to the government. *Id.* The government, rather than paying the retained sums to the insurance company, paid those monies to the Bankruptcy Court Trustee. The insurer objected and asserted that it had a priority interest in those funds.

Agreeing with the insurer and ordering payment to the insurance company, the Supreme Court held that "a surety who pays the debt of another is entitled to all the rights of the person he paid to enforce his right to be reimbursed. This rule is generally known as the right of subrogation." 371 U.S. at 137. Although there was no subrogation provision in the surety bonds issued to the construction company, the Court held that the insurer had a right of equitable subrogation. *Id.*

In review of its determination that the insurer had a subrogation right, the Court further stated that "property interests in a fund not owned by a bankrupt at the time of adjudication...are not a part of the bankrupt's property and do not vest in the trustee." *Id.* at 135. Consequently, the "Bankruptcy Act simply does not authorize a trustee to distribute other people's property among a bankrupt's creditors." *Id.* at 136. *Accord, In re DuBose*, 174 B.R. 260 (Bankr. N.D. Ohio 1994) (funds recovered by an insurer under a subrogation clause did not, under *Pearlman*, become part of the bankrupt insured's estate).

These principles apply to the dispute in this case.[2] The fact that Anthem's claim rises from contract, rather than equability, strengthens its claim. That claim is for $3,000, which is substantially less than the $100,000 sought by the Bergmans from the tortfeasor. In accordance with *Pearlman*, Anthem is entitled to recover the monies it expended for the Bergmans' medical expenses in the event that the Bermans prevail in their personal injury suit. Those funds cannot become property of the bankruptcy estate because that would enable the Trustee to distribute Anthem's property among the Bergmans' creditors, which the Bankruptcy Code does not authorize.

The Trustee argues that the Bankruptcy Code should be read narrowly, and that health insurance providers are not listed as entities entitled to priority status. The Trustee argues, furthermore, that medical payments made on behalf of debtors do not constitute "exceptional circumstances," such that they do not warrant priority status above a general unsecured creditor.

So far as they go, these contentions are indisputable: but they are misfocused, and fail to acknowledge the subrogation clause and the rights that arise under *Pearlman*.

Conclusion

In the light of the foregoing, it is

ORDERED THAT

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[2] Since the adoption of the Bankruptcy Code in 1978, the Bankruptcy Court for the Northern District of Ohio has held in accordance with *Pearlman*. *In re Dubose*, 174 B.R. 260 (Bankr. N.D. Ohio 1994).

1. Trustee's motion for judgment on the pleadings be, and the same hereby is denied;

2. Defendant's cross-motion for summary judgment be, and the same hereby is granted: all money, up to $3,000, that debtors recover in their civil suit shall be paid directly to defendant and shall not become property of the bankruptcy estate.

So ordered.

/s/James G. Carr
James G. Carr
United States District Judge

[Electronically file stamped 09/22/2005]